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Before the

House Ways and Means Committee

Hearing on:

Tax Ramifications of the Supreme Court's Ruling on the Democrats' Health Care Law

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Chairman Camp, Ranking member Levin, and members of the Committee, I am honored to testify before you today about the issues raised by the new taxing power recently described by the Supreme Court in *NFIB* v. *Sebelius*.

The Supreme Court's decision upholding the Patient Protection and Affordable Care Act was surprising to veteran court-watchers because it upheld the individual mandate based on a theory that no other court had accepted: that the mandate operated as a tax individuals may choose to pay in lieu of purchasing health insurance. That the parties themselves spent only a small percentage of their time addressing the tax issue in their briefs and at oral argument suggests that they too saw the issue as unlikely to get very far, yet it ultimately carried the day by a 5-4 vote.

When a case as major as this one is decided on a novel theory that has been so minimally argued, there is a risk that the majority may not have fully anticipated the ramifications of their decision. Unfortunately, the new tax authority described by the Court has implications that are nearly as pernicious for our constitutional structure as the Commerce Clause arguments that got all the attention before the decision.

The majority's interpretation of the taxing power is simply unprecedented in that it creates a new species of tax with chameleon-like properties.

Historically taxes and penalties were considered mutually exclusive. Indeed, the *NFIB* decision itself treats them as such, and establishes the mandate as a tax by saying that it did not really penalize because the consequences for non-compliance resulted in a relatively low mandatory payment and because there is no requirement that violators know

they are doing something wrong. But the Court did not stop there. Although it said that the mandate operated as a tax in order to avoid being struck down, it also held that it operated as a penalty in order to avoid falling under the Tax Injunction Act (which would have deprived the Court of the ability to decide the case before 2014). For the first time, an Act of Congress is a tax and not a tax at the same time.

Additionally, the opinion creates a previously unheard-of form of tax that is triggered by mere *inactivity*.

Taxes are primarily designed to raise revenue and only secondarily to influence behavior. With few exceptions, when Congress has deployed the taxing power to incentivize behavior, it has always been as a carrot, not a stick. Thus tax credits and deductions are given for such favored activities as raising children, purchasing a home, getting an education, hiring those who have been on long-term public assistance, or driving a hybrid car. And even where the federal government has used taxes as a stick to change behavior, such as taxing alcohol to reduce consumption, people have had to do some act in order for the tax to apply. But under the *NFIB* decision, for the first time Americans *will have to act* in order for the tax *not* to apply.

During the pendency of the case, many courts and commentators noted the problems of extending the Commerce Clause to allowing regulation of inactivity because the extension lacked any limiting principle. The Chief Justice's opinion recognizes this problem and notes that for this reason the distinction between activity and inactivity under the Commerce Clause has been respected through 200 years of American history.

But even under the Constitution's broad taxing power the same distinction holds. The Constitution allows taxes on activities, such as the capital gains tax, which is triggered

when you sell property at a gain. It also allows taxes on inactivity, through "direct" or "head" taxes. But the Constitution itself strictly limits direct taxes by requiring that they be apportioned among the states. Indeed, the majority opinion clearly acknowledges that the mandate affects the states unevenly and could not pass constitutional muster as a direct tax. Caught in this bind, the Court simply declared that the mandate operated as a never-before-seen tax: a tax on inactivity that doesn't need to be apportioned.

This move triggers the most damaging consequence of the *NFIB* decision: a massive expansion of the federal tax power. As a result, we must again consider whether the federal government can require people to purchase broccoli, this time by another means.

Allowing unrestricted taxes on inactivity will open the door to taxes the likes of which this country has never seen. For example, since seatbelts and motorcycle helmets increase road safety, Congress could simply tax those who refuse to wear them. Because "preventative services" are now required to be covered by all health insurance plans without co-pays, Congress might tax people who fail to take advantage of them. Rather than leaving it to municipalities to incentivize recycling, the federal government could tax those who fail to do so. Legislators could even tax anyone who does not own a gun, citing studies that gun ownership reduces crime. And forget tax incentives for installing solar panels. Congress can now just impose a tax on any American who refuses to buy them.

Whether any of these proposals are good or bad public policy is beside the point. The point is that Congress can levy any or all of these taxes in the wake of the *NFIB* decision.

Another consequence of the decision will likely be an uneven application of the taxing power by the lower courts because of the difficulty of administering the *NFIB* decision's standards. This is because the test laid out by the majority opinion for whether a

required payment qualifies as a tax or a penalty under the Constitution is vague and internally inconsistent. What, for example, would be considered an exaction sufficiently high to become more of a penalty than a tax? What if the text of the statute clearly states that it is to be interpreted as a penalty and not a tax – does that even matter if the Supreme Court can engage in linguistic alchemy to transmute one into the other?

Finally, this new tax regime could dramatically erode democratic accountability.

The great Chief Justice Marshall recognized what the founders were keenly aware of, that "[a]n unlimited power to tax involves, necessarily, a power to destroy." *McCulloch* v. *Maryland*. As such, the Constitution's allocation of the taxing power was specifically designed to maximize the public accountability for this most dangerous power. The authority to initiate taxes was given to the House to keep it in the most representative and immediately accountable house of Congress. Not only are the seats in the House distributed proportionally according to population, Members must answer to the electorate with great regularity, so that their decisions to raise taxes would be subject to prompt review at the next general election.

It is practically undisputed that the health care law would have died in Congress if it were acknowledged by its backers to be a tax that hit heavily on the middle class. But in the wake of *NFIB*, Congress now has the ability to pass massive tax increases of virtually any sort without ever having to utter the "T-word." If elected officials are allowed to represent one thing to the people ("it's a penalty") and another to the courts ("it's a tax"), the democratic accountability envisioned by the Founders will have been lost.

But even where Congress acts with pure intentions, those intentions may not be respected by the courts, who may rewrite a statute in order to save it. That takes the tax

power out of the most representative branch and puts it into the judicial branch – the one purposely insulated from having to answer to the American people.

As we approach the point where there are no judicially enforceable limits on the enumerated powers of Congress, the most important limits on future legislators will be those they are willing to impose on themselves.